COBRA AND OTHER HEALTH CARE ISSUES

By

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I. INTRODUCTION

There has been a great deal of activity, both legislative and regulatory, in recent years in the group health plan area. In order to continue to provide health benefits, to ensure the desired tax effects are allowed and to avoid penalties, employers and plan administrators must comply with the various laws and regulations governing group health plans. This outline provides an overview of the COBRA continuation coverage requirements, a survey of recent legal developments affecting COBRA compliance, including the 1999, 2001, 2003 and 2004 regulations, and guidance on some of the common problems that have been identified by employers and plan administrators concerning the implementation of COBRA. The outline also discusses recent developments with regard to other health care issues, including a general summary of provisions affecting group health plans enacted from 1994 forward, such as the Uniformed Services Employment and Reemployment Rights Act of 1994 (“USERRA”), the Health Insurance Portability and Accountability Act of 1996 (“HIPAA”), the Small Business Job Protection Act of 1996 (“96 Act”), the Mental Health Parity Act of 1996 (“MHPA”), the Newborns’ and Mothers’ Health Protection Act of 1996 (“Maternity Act”), the Taxpayer Relief Act of 1997 (“97 Act”), the Child Support Performance and Incentive Act of 1998, the Women’s Health and Cancer Rights Act of 1998 (“Women’s Health Act”), the Tax and Trade Relief Extension Act of 1998 (“98 Act”), the Trade Act of 2002 (“Trade Act”) and the Medicare Prescription Drug Improvement and Modernization Act of 2003 (“2003 Act”). As outlined in this paper, HIPAA included a tremendous number of new requirements, amending the Employee Retirement Income Security Act of 1974 (“ERISA”), the Public Health Service Act (“PHSA”) and the Internal Revenue Code (“Code” or “I.R.C.”). Those requirements impact employers sponsoring group health plans covered by ERISA, health care providers and other service providers. Regulations and additional guidance have been issued each year subsequent to HIPAA’s enactment by the four governmental agencies (Internal Revenue Service, Department of the Treasury; Pension and Welfare Benefits Administration (renamed Employee Benefits Security Administration (“EBSA”)), Department of Labor; Health Care Financing and Administration (renamed Centers for Medicare and Medicaid Services (“CMS”)) and Office of Civil Rights, Department of Health and Human Services (“DHHS”)) charged with implementing HIPAA’s provisions. Because HIPAA includes various effective dates, we have already been impacted by some of the provisions and we have others that are not yet effective. There are more substantive issues than ever before that must be addressed in implementing and maintaining each group health plan.
II. COBRA REQUIREMENTS

A. HISTORICAL OVERVIEW

The Consolidated Omnibus Budget Reconciliation Act of 1986 ("COBRA"), which was enacted on April 7, 1986, was the first of several statutes enacted as a result of Congress’ concern with the growing number of Americans without health insurance coverage. COBRA amended the Code and ERISA to include continuation coverage requirements for employer provided group health plans. COBRA also amended the PHSA, which governs the health plans of state and local governments. The COBRA rules have been revised by the Tax Reform Act of 1986, the Technical and Miscellaneous Revenue Act of 1988 (TAMRA), the Omnibus Budget Reconciliation Act of 1989 (OBRA ‘89), the Omnibus Budget Reconciliation Act of 1990, the Omnibus Budget Reconciliation Act of 1993 (OBRA ‘93), the ‘96 Act, HIPAA and the Trade Act.

In addition, the Department of Treasury issued proposed regulations interpreting COBRA on June 15, 1987 and January 7, 1998; final regulations and new proposed regulations on February 3, 1999; and final regulations in 2001 supplementing and finalizing the 1999 regulations. The COBRA provisions in the Code were originally enacted as I.R.C. § 162(k). Until the 1998 and 1999 regulations, all of the COBRA regulations were at Prop. Treas. Reg. § 1.162-26. However, TAMRA deleted I.R.C. § 162(k) and added I.R.C. § 4980B, which is the current Code Section covering the COBRA continuation requirements. The 1998 proposed Treasury regulations were set forth in Section 54.4980B-1. The 1999 final Treasury regulations were set forth in Sections 54.4980B-1 through 54.4980B-8 and are applicable to "qualifying events" that occur in plan years beginning on or after January 1, 2000. The 1999 proposed Treasury regulations included proposed revisions to the 1999 final regulations and added additional provisions at Sections 54.4980B-9 and 54.4980B-10.

Prior to the effective date of the 1999 final Treasury regulations, plans were required to comply in good faith with a reasonable interpretation of the COBRA statutes and the 1987 and 1998 proposed regulations. The 2001 final Treasury regulations were effective January 10, 2001; they finalize and supplement the 1999 regulations and generally apply to the Code and ERISA for “qualifying events” and business reorganizations that occur on or after January 1, 2002. The 2001 final Treasury regulations also provide that for topics relating to COBRA that are not addressed in the regulations in Sections 54.4980B-1 through 54.4980B-10 (such as methods for calculating the applicable premium) plans and employers must operate in good faith compliance with a reasonable interpretation of the statutory requirements. The good faith standard will be effective for purposes of application of the excise tax under the Internal Revenue Code for failure to comply with COBRA. However, under Title I of ERISA the courts may not follow the good faith standard.

The Department of Labor also issued proposed regulations on May 28, 2003 and final regulations on May 26, 2004 that include guidance on compliance with COBRA notice provisions and model notices to be sent to employees, spouses and retirees covered under group health plans. The 2004 final Labor regulations are effective July 26, 2004 and apply to notice obligations under COBRA on or after the first day of the first plan year beginning on or
Both the Internal Revenue Service ("IRS") and the Department of Labor ("DOL") enforce the COBRA requirements. I.R.C. § 4980B imposes an excise tax for failure to comply with COBRA. Sections 601 through 609 of ERISA provide individuals and the Department of Labor with the right to compel a plan to comply with the COBRA provisions and provide for penalties against plan administrators who fail to comply with such provisions. In this outline, where the provisions of COBRA are identical in the Code and ERISA, the cite to the Code is generally utilized. In addition to the legislative and regulatory changes under COBRA, the courts have played a major role in the formation of the current state of the COBRA laws. The courts have generally interpreted unclear laws in favor of the employees and their dependents.

**B. GENERAL REQUIREMENTS**

Under COBRA, group health plans must continue to make coverage available to employees and their dependents who would, except for COBRA, lose benefits as a result of a certain "qualifying event." The continuation rules enacted by Congress as part of COBRA, provide employees and their dependents with transitional medical benefit coverage in the event of a change of employment or job status, and of certain changes in family status. COBRA continuation applies to the benefits provided under any group health plan that furnishes medical care benefits for employees and their dependents regardless of whether the plan is insured or self-funded. However, there are exceptions for certain government plans, for church plans, and for plans of a "small employer."

The continuation requirement is triggered by the occurrence of a "qualifying event." The period over which self-financed coverage must be extended depends on the qualifying event, as well as the qualified beneficiary. Under COBRA, employers and plan administrators have significant obligations to notify employees and other qualified beneficiaries of their continuation rights and must allow such persons a specified time frame during which an election to continue coverage may be made. As a result of the statutory election period, a plan may be responsible for paying benefits retroactively. Also, failure to comply with COBRA may result in tax penalties and liability for payment of benefits not otherwise required. To ensure COBRA compliance, employers should implement and update training procedures, provide written instructions for those performing the compliance functions, have compliance audits performed or monitored by independent auditors, consult with legal counsel before denying continuation coverage and execute detailed service agreements with third party administrators providing COBRA administration services.

**C. PLANS WHICH MUST COMPLY WITH COBRA**

Section 601(a) of ERISA and Section 4980B(f) of the Code require the plan sponsor of each group health plan to provide continuation coverage under the plan. I.R.C. § 4980B(g)(2) refers to I.R.C. § 5000(b)(1) for purposes of defining a “group health plan.” I.R.C. § 5000(b)(1) defines a “group health plan” as a plan, including a self-insured plan, of...
or contributed by to an employer (including a self-employed person) or an employee organization, to provide health care (directly or otherwise) to the employees, former employees, the employer, others associated or formerly associated with the employer in a business relationship, or their families. The 2001 final Treasury regulations generally refer to all individuals covered under a plan by virtue of the performance of services or by virtue of membership in an employee organization as employees. For this purpose, employer includes (1) a person for whom an individual performs services and (2) with respect to the person, any member of a group described in I.R.C. §§ 414(b), (c), (m) or (o) (Controlled Group), as well as any successor of the person or of a member of the Controlled Group. COBRA is applicable to health care offered under cafeteria plans only with respect to individuals who actually receive health care coverage under the plan. Government plans and church plans as defined in I.R.C. §§ 414(d) and (e), respectively, are not subject to the COBRA requirements. However, state and local governments must comply with parallel requirements under the PHSA and federal employees are entitled to similar continuation coverage under the Federal Employees Health Benefits Amendment Act of 1988. Also, church plans may be subject to similar continuation coverage requirements under state law.

1. **Small Employer Exception.** I.R.C. § 4980B(d)(1) provides that COBRA does not apply to a group health plan with respect to any qualified beneficiary where the qualifying event with respect to the beneficiary occurred during the calendar year immediately following a calendar year during which all employers maintaining the plan normally employed fewer than twenty (20) employees on a typical business day.

   a. Prior to the effective date of the 1999 final Treasury regulations, Prop. Treas. Reg. § 1.162-26 Q&A - 9(b) clarified that an employer was considered as having normally employed fewer than 20 employees during a particular calendar year only if it had fewer than 20 employees on at least 50% of its working days during that year. In determining the number of employees, an employer was to treat as employees all full-time and part-time employees and all self-employed employees within the meaning of I.R.C. § 401(c)(1). An employer was also to treat as employees all agents, independent contractors and directors if such individuals were eligible to participate in a group health plan maintained by the employer. Prop. Treas. Reg. § 1.162-26 Q&A 9(C). The 1999 and 2001 Treasury regulations substantially changed how the small employer exception is calculated.

   (1) A plan maintained by a single employer is now a small employer plan if the employer normally employed less than 20 common law employees on a typical business day during the preceding calendar year. This requirement is met only if the employer had less than 20 common law employees on at least 50% of its typical business days during that calendar year. All full-time and part-time common law employees are taken into account. Even
though self-employed individuals, independent contractors and their employees, and directors are treated as employees for all other purposes under the final 1999 and 2001 Treasury regulations, they are not counted as employees for purposes of calculating the number of employees in making the small employer plan determination. Treas. Reg. § 54.4980B-2 Q&A-5(b) and (c).

(2) Each full-time employee is treated as one employee and each part-time employee is counted as a fraction of an employee. Treas. Reg. § 54.4980B-2 Q&A-5(d).

(3) An employer may determine the number of employees on a daily basis or a pay period basis. Treas. Reg. § 54.4980B-2 Q&A-5(e).

(a) If an employer makes the determination on a daily basis, the numerator in the fraction is the number of hours a part-time employee works on a typical business day and the denominator is the number of hours a full-time employee works on a typical business day in order to be considered full-time.

(b) For a pay period basis determination, the numerator is the number of hours a part-time employee works in a pay period and the denominator is the number of hours a full-time employee works during the pay period in order to be considered full-time. The number of hours to be considered full-time is based on the employer’s employment practices, but the hours required may not exceed 8 hours for any day or 40 hours for a week.

(c) For example, an employer making a determination on a daily basis, with 10 employees working part-time four hours a day and 10 employees working full-time eight hours a day, would be considered to have 15 employees for that business day.

(d) For an employer making a determination on a pay period basis that pays weekly, 10 employees working part-time 20 hours a week and 10 employees working full-time 40 hours a week would be considered to have 15 employees for that pay period.

(4) The basis used by the employer must be used with respect to all employees and must be used for the entire year. Treas. Reg. § 54.4980B-2 Q&A-5(e).